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Flagrant Foul by the Federal Trade Commission: Revising the Horizontal Merger Guidelines in the Wake of the Blocked DraftKings and FanDuel Merger

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Comments

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I. INTRODUCTION

Imagine founding a company that revolutionizes the way people enjoy professional sports.[1] Then, after seven years of being in business, the company has yet to achieve profitability, due in large part to the exorbitant legal expenses required to lobby for and defend the legality of the company's nascent industry.[2] Consequently, to help ensure the survival of the company, you do the unthinkable—agree to merge with your bitter rival.[3]

This was the situation confronting FanDuel, a major daily fantasy sports ("DFS") company, in November 2016 when it announced an agreement to merge with DraftKings (the "Merger").[4] Pending regulatory approval from the Federal Trade Commission ("FTC" or "Commission"), the companies expected to consummate the Merger by the end of 2017.[5] Ultimately, FanDuel and DraftKings never received that approval.[6] Instead, the FTC elected to challenge the Merger due to competition concerns.[7] As a result, in July 2017, FanDuel and DraftKings decided to terminate their pursuit of a merger, rather than spend

1. *See generally About*, FANDUEL, https://www.fanduel.com/about (last visited Oct. 31, 2017) (on file with *The University of the Pacific Law Review*) (discussing the founding of FanDuel).

2. *See* Darren Heitner, *How and Why FanDuel and DraftKings Decided to Merge*, FORBES (Nov. 18, 2016), https://www.forbes.com/sites/darrenheitner/2016/11/18/how-and-why-fanduel-and-draftkings-decided-to-merge/#340fa7687c45 (on file with *The University of the Pacific Law Review*) (revealing that FanDuel "spent almost $8 million in legal fees" during the fourth quarter of 2015).

3. *See* David Purdum, *Planned Merger Between DraftKings, FanDuel Is Off*, ESPN (July 14, 2017), http://www.espn.com/chalk/story/_/id/20002903/in-abrupt-fashion-draftkings-fanduel-merger-off (on file with *The University of the Pacific Law Review*) (questioning "whether both DraftKings and FanDuel can survive as separate entities").

4. *Id.*

5. Heitner, *supra* note 2.

6. Purdum, *supra* note 3.

7. *Id.*

upwards of $15 million on another legal battle.[8]

The FTC and some industry commentators view this result as "a major win for daily fantasy sports consumers."[9] This Comment, however, argues that critical flaws in the FTC's analysis not only led to an incorrect decision to challenge the Merger, but also demonstrate the need to consider revising the Commission's Horizontal Merger Guidelines ("Guidelines").[10] The Guidelines are the analytical framework the FTC uses to determine whether to challenge a particular horizontal merger.[11] The FTC should revise the Guidelines because, as the DraftKings and FanDuel experience reveals, the FTC may not be accomplishing its "mission to protect consumers and promote competition" as effectively as it otherwise could, which has far-reaching implications for consumers and industries across the country.[12]

Part II discusses the FTC's authority to review horizontal mergers and the Guidelines.[13] Part III examines the administrative complaint the FTC filed challenging the proposed Merger.[14] Part IV analyzes the critical flaws in the FTC's rationale for contesting the Merger, which led the FTC to unnecessarily challenge the Merger.[15] Finally, Part V offers potential revisions to the Guidelines that will address the shortcomings of the current version of the Guidelines.[16] The Guidelines must be reevaluated in light of the FTC's analytical missteps with the Merger.[17]

II. THE REFEREE AND RULEBOOK FOR REVIEWING HORIZONTAL MERGERS

Before discussing the particulars of the failed Merger, this Comment explores the relevant regulatory framework for reviewing horizontal mergers in the United States.[18] Section A describes the FTC's statutory authorization to

8. *Id.*

9. Marc Edelman, *FTC Challenges Proposed DraftKings and FanDuel Merger: A Win for Daily Fantasy Consumers*, FORBES (June 19, 2017), https://www.forbes.com/sites/marcedelman/2017/06/19/ftc-challenges-proposed-draftkings-and-fanduel-merger-a-win-for-daily-fantasy-consumers/#241e0acb4698 (on file with *The University of the Pacific Law Review*).

10. *Infra* Parts IV–V.

11. DEP'T OF JUST. & FED. TRADE COMM'N, HORIZONTAL MERGER GUIDELINES 1 (2010), *available at* https://www.ftc.gov/sites/default/files/attachments/merger-review/100819hmg.pdf [hereinafter GUIDELINES] (on file with *The University of the Pacific Law Review*).

12. *What We Do*, FED. TRADE COMM'N, https://www.ftc.gov/about-ftc/what-we-do (last visited Nov. 7, 2017) (on file with *The University of the Pacific Law Review*).

13. *Infra* Part II.

14. *Infra* Part III.

15. *Infra* Part IV.

16. *Infra* Part V.

17. *Infra* Parts IV–V.

18. *Infra* Part II. The Antitrust Division of the U.S. Department of Justice ("DOJ") also plays an important role in "enforc[ing] the federal antitrust laws," but, because the FTC handled the investigation into the proposed Merger, this Comment does not address the DOJ's role in reviewing mergers. *The Enforcers*, FED. TRADE COMM'N, https://www.ftc.gov/tips-advice/competition-guidance/guide-antitrust-laws/enforcers (last

review horizontal mergers.[19] Section B discusses the FTC's Guidelines for challenging a horizontal merger.[20]

A. The Referee: The Federal Trade Commission's Authority to Review Horizontal Mergers

The FTC challenged the proposed Merger pursuant to the authority vested in the FTC by the Clayton Act and the Federal Trade Commission Act ("FTC Act").[21] The Clayton Act proscribes corporate acquisitions that are likely to result in substantially less competitive markets.[22] The statute vests the authority to enforce this provision in the FTC.[23] If the FTC determines that a proposed merger is inconsistent with the Clayton Act and the merging companies refuse to abandon the merger, the FTC may challenge the merger by "issu[ing] an administrative complaint and/or seek[ing] injunctive relief in the federal courts."[24]

The FTC Act expands the Commission's authority by allowing it "to address acts or practices that are anticompetitive but may not fall within the scope of the . . . Clayton Act."[25] The FTC Act declares that "[u]nfair methods of competition in or affecting commerce" are unlawful, and empowers the FTC to ensure corporations do not engage in such conduct.[26] If the Commission believes a proposed merger would violate the FTC Act, it may initiate an administrative adjudicatory action under the FTC Act.[27] The adjudicatory proceedings under the FTC Act parallel the proceedings initiated under the Clayton Act.[28] Enforcing these statutes helps the Commission achieve its goal of "ensur[ing] that [American] markets are open and free" and "work[] according to consumer preferences, not illegal practices."[29]

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visited Nov. 7, 2017) (on file with *The University of the Pacific Law Review*).

19. *Infra* Part II.A.

20. *Infra* Part II.B.

21. 15 U.S.C.A. §§ 18, 45 (Westlaw through Pub. L. No. 115-72).

22. *Id.*

23. 15 U.S.C.A. § 21(a) (Westlaw through Pub. L. No. 115-72).

24. *The Enforcers*, *supra* note 18.

25. Donald S. Clark, Secretary, *Statement of Enforcement Principles Regarding "Unfair Methods of Competition" Under Section 5 of the FTC Act*, FED. TRADE COMM'N (Aug. 13, 2015), *available at* https://www.ftc.gov/system/files/documents/public_statements/735201/150813section5enforcement.pdf (on file with *The University of the Pacific Law Review*).

26. 15 U.S.C.A. § 45(a)(1)–(2) (Westlaw through Pub. L. No. 115-72).

27. *A Brief Overview of the Federal Trade Commission's Investigative and Law Enforcement Authority*, FED. TRADE COMM'N (July 2008), https://www.ftc.gov/about-ftc/what-we-do/enforcement-authority (on file with *The University of the Pacific Law Review*).

28. *Id.*

29. *What We Do*, *supra* note 12.

B. The Rulebook: The Horizontal Merger Guidelines

The Guidelines reflect "the principal analytical techniques and the main types of evidence on which the [FTC] usually rel[ies] to predict whether a horizontal merger may substantially lessen competition."[30] Thus, the Guidelines are key to the FTC's merger review process.[31] If, according to the Guidelines, a merger is likely to substantially lessen competition, the FTC will almost certainly challenge the merger.[32]

This Section generally describes portions of the Guidelines that appeared prominently in the FTC's decision to challenge the Merger.[33] Subsection 1 discusses how the Guidelines approach product market definition and how this affects the market concentration analysis.[34] Subsection 2 focuses on potential anticompetitive effects mergers have on customers and industries.[35] Subsection 3 explores how market entry can mitigate a merger's anticompetitive effects.[36] Finally, Subsection 4 explains how the FTC could be persuaded to approve a merger if the merging firms can substantiate cognizable efficiencies that will result from the merger.[37]

1. Product Market Definition and Market Concentration

Defining the relevant product market is an important function of the Guidelines because it "allows the [FTC] to identify market participants and measure market shares and market concentration."[38] The analysis concentrates on demand substitution factors.[39] In other words, the analysis seeks to identify "customers' ability and willingness to substitute away from one product to another in response to a price increase or a corresponding non-price change such as a reduction in product quality or service."[40] The FTC engages with customers to ensure it properly defines the product market, as "[c]ustomers are typically the best source . . . of critical information on the factors that govern their ability and

30. GUIDELINES, *supra* note 11, at 1.

31. FED. TRADE COMM'N, TRANSCRIPT OF THE HORIZONTAL MERGER GUIDELINES REVIEW PROJECT 15 (Dec. 3, 2009), *available at* https://www.ftc.gov/sites/default/files/documents/public_events/horizontal-merger-guidelines-review-project/091203transcript.pdf [hereinafter GUIDELINES REVIEW PROJECT TRANSCRIPT] (on file with *The University of the Pacific Law Review*). Robert Pitofsky, former Chairman of the FTC, asserted the Guidelines have "had the most important influence on American antitrust policy in the last 50 years." *Id.*

32. 15 U.S.C.A. § 18 (Westlaw through Pub. L. No. 115-72).

33. *Infra* Part II.B.

34. *Infra* Part II.B.1.

35. *Infra* Part II.B.2.

36. *Infra* Part II.B.3.

37. *Infra* Part II.B.4.

38. *See* GUIDELINES, *supra* note 11, at 7 (describing the important reasons behind market definition).

39. *Id.*

40. *Id.*

willingness to substitute in the event of a price increase."[41]

The FTC applies the hypothetical monopolist test to accurately establish the relevant product market.[42] This test "requires that a product market contain enough substitute products so that it could be subject to post-merger exercise of market power significantly exceeding that existing absent the merger."[43] The test safeguards against defining a relevant product market too narrowly.[44]

Defining the relevant product market is important because it allows the FTC to undertake a market concentration analysis.[45] The FTC's calculation of the Herfindahl-Hirschman Index ("HHI") often sheds light on a merger's likely competitive effects.[46] The Commission calculates the HHI "by summing the squares of the individual firms' market shares, and thus gives proportionately greater weight to the larger market shares."[47] As part of this analysis, the FTC "consider[s] both the post-merger level of market concentration and the change in concentration resulting from a merger."[48]

In some instances, the HHI calculation carries significant weight.[49] If the FTC concludes "the post-merger level of the HHI and the increase in the HHI resulting from the merger" are sufficiently high, the FTC will declare the merger to be presumptively illegal.[50] Mergers that result in a post-merger HHI level above 2,500 and "an increase in the HHI of more than 200 points" are presumptively illegal.[51] Despite this presumption, the Guidelines state that "[t]he purpose of these thresholds is not to provide a rigid screen to separate competitively benign mergers from anticompetitive ones."[52] Instead, the Commission intends for the HHI calculation to be "one way to identify some mergers unlikely to raise competitive concerns and some others for which it is particularly important to examine whether other competitive factors confirm, reinforce, or counteract the potentially harmful effects of increased concentration."[53] For these reasons, defining the product market and measuring market concentration are critical aspects of the Guidelines.[54]

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41. DEP'T OF JUST. & FED. TRADE COMM'N, COMMENTARY ON THE HORIZONTAL MERGER GUIDELINES 9 (2006), *available at* https://www.ftc.gov/sites/default/files/attachments/merger-review/commentaryonthehorizontalmergerguidelinesmarch2006.pdf (on file with *The University of the Pacific Law Review*).

42. GUIDELINES, *supra* note 11, at 8–9.

43. *Id.* at 9.

44. *Id.*

45. *Id.* at 7.

46. *Id.* at 18.

47. *Id.*

48. *Id.*

49. *Id.* at 19.

50. *Id.*; Complaint, DraftKings, Inc. (dismissed July 14, 2017) (No. 9375), 2017 WL 3049123 (F.T.C.), at *8.

51. GUIDELINES, *supra* note 11, at 19.

52. *Id.*

53. *Id.*

54. *Id.*

2. Anticompetitive Effects

When two competing firms merge, "[t]he elimination of competition between [them] that results from their merger may alone constitute a substantial lessening of competition."[55] The Guidelines term this result as a merger's "unilateral effects," which can take various forms.[56] For example, a merger "may diminish competition by enabling the merged firm to profit by unilaterally raising the price of one or both products above the pre-merger level."[57] Reduced competition also may incentivize a "merged firm to curtail its innovative efforts below the level that would prevail in the absence of the merger."[58] A merged firm, for example, may have "reduced incentive to continue with an existing product-development effort or reduced incentive to initiate development of new products."[59] Finally, a merger could lead to less product variety.[60] This lack of product variety could be harmful to consumers if the merged firm removes products most consumers strongly prefer to what would remain available in the marketplace.[61] If the FTC believes any of these harmful unilateral effects are likely to result from a merger's substantial reduction in competition, the FTC will likely challenge the merger.[62]

3. Market Entry

The Guidelines also recognize that "[t]he prospect of entry into the relevant market will alleviate concerns about adverse competitive effects[, but] only if such entry will deter or counteract any competitive effects of concern so the merger will not substantially harm consumers."[63] To determine if market entry may counteract anticompetitive effects, the FTC analyzes the "timeliness, likelihood, and sufficiency of the entry efforts an entrant might practically employ."[64] Entry is timely if it is "rapid enough that customers are not significantly harmed by the merger, despite any anticompetitive harm that occurs prior to the entry."[65] The Guidelines also indicate that "[e]ntry is likely if it would be profitable, accounting for the assets, capabilities, and capital needed and the risks involved, including the need for the entrant to incur costs that would

55. *Id.* at 20.
56. *Id.*
57. *Id.*
58. *Id.* at 23.
59. *Id.*
60. *Id.* at 24.
61. *Id.*
62. 15 U.S.C.A. § 18 (Westlaw through Pub. L. No. 115-72).
63. GUIDELINES, *supra* note 11, at 28.
64. *Id.*
65. *Id.* at 29.

not be recovered if the entrant later exits."[66] Finally, entry is sufficient if it is capable of counterbalancing a merger's anticompetitive effects.[67]

As part of its market entry analysis, the FTC "consider[s] the actual history of entry into the relevant market and give[s] substantial weight to this evidence."[68] This history is important because a "[l]ack of successful and effective entry in the face of non-transitory increases in the margins earned on products in the relevant market tends to suggest that successful entry is slow or difficult."[69] The Guidelines recognize that obtaining accurate and thorough information may be extremely difficult and, therefore, "the [FTC] consider[s] reasonably available and reliable evidence bearing on whether entry will satisfy the conditions of timeliness, likelihood, and sufficiency."[70]

4. Efficiencies

Finally, the Guidelines recognize that mergers have the "potential to generate significant efficiencies and thus enhance the merged firm's ability and incentive to compete, which may result in lower prices, improved quality, enhanced service, or new products."[71] While recognizing this potential, however, the Guidelines assert that "[e]fficiencies are difficult to verify and quantify," and "credit only those efficiencies likely to be accomplished with the proposed merger and unlikely to be accomplished in the absence of either the proposed merger or another means having comparable anticompetitive effects."[72] The Commission places the burden "upon the merging firms to substantiate efficiency claims so that [the Commission] can verify by reasonable means the likelihood and magnitude of each asserted efficiency."[73] Further, the merging firms must demonstrate "how and when each [efficiency] would be achieved (and any costs of doing so), how each would enhance the merged firm's ability and incentive to compete, and why each would be merger-specific."[74]

In the end, the Guidelines play a key role in antitrust law enforcement.[75] Not only do the Guidelines anchor the FTC's merger analysis and enforcement, they also serve the important purpose of "provid[ing] greater transparency and foster[ing] deeper understanding regarding antitrust law enforcement."[76] For these reasons, the effectiveness of the FTC's merger enforcement and the welfare

66. *Id.*
67. *Id.*
68. *Id.* at 28.
69. *Id.*
70. *Id.*
71. *Id.* at 29.
72. *Id.* at 30.
73. *Id.*
74. *Id.*
75. *See* GUIDELINES REVIEW PROJECT TRANSCRIPT, *supra* note 31, at 15.
76. GUIDELINES, *supra* note 11, at 1.

of American businesses and consumers hinge on the soundness of the Guidelines.[77]

III. BLOWING THE WHISTLE: THE FEDERAL TRADE COMMISSION'S COMPLAINT AGAINST THE DRAFTKINGS AND FANDUEL MERGER

On June 19, 2017, the Commission filed an administrative complaint to challenge the Merger.[78] The following Sections describe the FTC's main reasons for challenging the Merger.[79] Section A discusses how the FTC defined the relevant product market DraftKings and FanDuel compete in.[80] Section B explores the FTC's finding that the Merger, if consummated, would have significant anticompetitive effects.[81] Finally, Section C describes the Commission's determination that there were no countervailing factors to convince the Commission to approve the Merger.[82]

A. Defining the Relevant Product Market

The FTC determined that paid DFS is "a distinct relevant product market" and used this as support for its decision to challenge the Merger.[83] The Commission reached this conclusion because it found important distinctions between paid DFS and other types of fantasy sports, such as season long fantasy sports ("SLFS").[84] For example, according to the FTC, DFS and SLFS are different because DFS contests have a much shorter duration.[85] Additionally, the two contests are different because "SLFS participants play primarily for social reasons," while the opportunity for financial gain motivates DFS participants.[86] Finally, DFS and SLFS generally have different contest sizes because, unlike DFS contests, SLFS games do not allow an athlete to appear on multiple teams at the same time.[87] For these reasons, the FTC concluded SLFS contests "are not sufficiently substitutable to belong in a paid DFS relevant product market."[88]

Based on this conclusion, the FTC excluded SLFS from its market

77. *Id.*

78. Press Release, *FTC and Two State Attorneys General Challenge Proposed Merger of the Two Largest Daily Fantasy Sports Sites, DraftKings and FanDuel*, FED. TRADE COMM'N (June 19, 2017), https://www.ftc.gov/news-events/press-releases/2017/06/ftc-two-state-attorneys-general-challenge-proposed-merger-two (on file with *The University of the Pacific Law Review*).

79. *Infra* Part III.A–C.

80. *Infra* Part III.A.

81. *Infra* Part III.B.

82. *Infra* Part III.C.

83. Complaint, DraftKings, Inc. (dismissed July 14, 2017) (No. 9375), 2017 WL 3049123 (F.T.C.), at *5.

84. *Id.*

85. *Id.*

86. *Id.*

87. *Id.* at *6.

88. *Id.* at *5.

concentration analysis.[89] As a result, the Commission determined that the Merger would lead to a highly concentrated DFS market.[90] The Commission calculated that "the Merger would result in a post-Merger HHI of at least 8,100 and an increase in concentration much greater than 200 points."[91] These HHI levels prompted the Commission to declare the Merger presumptively unlawful.[92]

B. The Merger's Anticompetitive Effects

The FTC also found that the Merger would have significant anticompetitive effects.[93] For example, the Commission believed approving the Merger would result in "higher commission rates and lower promotional offers."[94] According to the Commission, this would occur because DraftKings currently serves as an important constraint on FanDuel's ability to raise prices, and vice versa.[95] The FTC reasoned that this price competition would no longer exist after the Merger, leading to higher prices for customers.[96]

Additionally, the FTC contended the Merger would eliminate non-price competition.[97] As separate entities, DraftKings and FanDuel compete on non-price factors such as contest size, product features, and sports offerings.[98] If the FTC allowed the companies to merge, the merged company "would have significantly less incentive to maintain and to improve the quality of its contest offerings and user experience."[99] From the Commission's perspective, this reduction in product quality and incentive to innovate would harm consumers, making this an important anticompetitive effect of the Merger.[100]

C. Lack of Countervailing Factors

Finally, the Commission asserted there were no countervailing factors that would counterbalance the Merger's anticompetitive effects.[101] For example, the FTC contended new entrants into the paid DFS market would be unlikely because of significant barriers to entry, such as regulatory uncertainty and

89. *Id.*
90. *Id.* at *7.
91. *Id.* at *8.
92. *Id.*
93. *Id.* at *8–9.
94. *Id.* at *8.
95. *Id.* at *9.
96. *Id.* at *10.
97. *Id.* at *2.
98. *Id.* at *10.
99. *Id.*
100. *Id.*
101. *Id.* at *12.

compliance costs.[102] Additionally, the FTC found that the Merger created no cognizable efficiencies "that rebut the strong presumption and evidence that the Merger likely would substantially lessen competition in the relevant market."[103] The FTC also concluded neither DraftKings nor FanDuel is in danger of going out of business, which would have militated in favor of approving the Merger.[104] Because the Commission found no factors that would counteract the Merger's significant anticompetitive effects, it filed an administrative complaint to challenge the Merger.[105]

IV. REVIEWING THE CALL ON THE COURT: THE FEDERAL TRADE COMMISSION'S ANALYTICAL MISSTEPS

The FTC insists it is protecting American consumers by challenging the Merger, and some industry experts have commended the FTC for its actions.[106] After further review, there are numerous flaws in the Commission's analysis of the Merger.[107] These flaws played an important role in the FTC's decision to challenge the Merger, and analyzing them reveals the FTC should not have challenged the Merger.[108] Section A argues the FTC mischaracterized the relevant product market, leading it to overstate the Merger's anticompetitive effects and incorrectly apply the presumption of illegality.[109] Section B describes the important countervailing factors the FTC dismissed when analyzing the Merger.[110]

A. Mischaracterizing the Relevant Product Market

The FTC determined the differences between DFS and SLFS are sufficient to make paid DFS "a distinct relevant product market."[111] With the exclusion of SLFS, the Commission mischaracterized the relevant product market because the differences between the two are not as significant as the Commission asserts.[112] First, the FTC contends the markets are different because DFS players primarily

102. *Id.* at *13.
103. *Id.* at *14.
104. *Id.* at *13.
105. *Id.*
106. Edelman, *supra* note 9.
107. *Infra* Part IV.A–B.
108. *Infra* Part IV.A–B.
109. *Infra* Part IV.A.
110. *Infra* Part IV.B.
111. Complaint, DraftKings, Inc. (dismissed July 14, 2017) (No. 9375), 2017 WL 3049123 (F.T.C.), at *5.
112. FANTASY SPORTS TRADE ASSOCIATION, ONE-DAY VS. SEASON-LONG FANTASY PLAYERS: IS THERE A DIFFERENCE? 10 (2015), *available at* http://www.fstaconference.com/docs/09-McClain-Eggles-Demographics.pdf (on file with *The University of the Pacific Law Review*).

participate to win money, while SLFS users play to interact with friends.[113] This argument distinguishes between the markets by overstating the importance of financial gain to DFS players and understating the importance to SLFS users.[114] Industry data demonstrates the opportunity for financial gain is not the primary motivation for most DFS players.[115] In one study, for example, only 13.3% of DFS players stated profit is the main reason for playing DFS.[116] Rather than profit, many DFS players reported excitement, competition, and strategy as being primary motivators for engaging in DFS.[117]

Industry data also demonstrates that the FTC overlooked the importance of financial gain to SLFS users.[118] For example, 43% of SLFS players list financial gain as one of the reasons for playing SLFS.[119] Additionally, industry data from 2016 reveals that the average SLFS player spent $184 on SLFS over a one-year period.[120] While this trails the $318 an average DFS player spent on his or her games over the same time period, the spending on SLFS and motivation to win money are not insignificant.[121] Thus, the DFS and SLFS markets are more similar than different because the opportunity for financial gain is an important motivation for players in both markets.[122]

Additionally, the Commission insisted that the DFS and SLFS markets are distinct because not many DFS players are interested in playing SLFS.[123] According to the FTC, "most DFS users are not likely to turn to SLFS as a substitute product in response to a small but significant price increase."[124] Once again, industry data refutes this claim.[125] An industry study found 82.8% of DFS users also play traditional SLFS, meaning the two contests frequently compete for the same consumers.[126] As a result, SLFS and DFS consumers are not as different as the Commission argues.[127]

The companies' decisions to begin offering games that closely resemble traditional SLFS offerings further complicate the decision to label DraftKings

113. Complaint, *supra* note 50, at *5.

114. FANTASY SPORTS TRADE ASSOCIATION, *supra* note 112, at 10, 12.

115. *Id.* at 12.

116. *Id.*

117. *Id.*

118. *Id.* at 10.

119. *Id.*

120. *Industry Demographics*, FANTASY SPORTS TRADE ASS'N, https://fsta.org/research/industry-demographics/ (last visited Dec. 28, 2017) (on file with *The University of the Pacific Law Review*).

121. *Id.*

122. FANTASY SPORTS TRADE ASSOCIATION, *supra* note 112, at 10.

123. Complaint, DraftKings, Inc. (dismissed July 14, 2017) (No. 9375), 2017 WL 3049123 (F.T.C.), at *6.

124. *Id.* at *7.

125. FANTASY SPORTS TRADE ASSOCIATION, *supra* note 112, at 10.

126. *Id.* at 9.

127. *Id.* at 10.

and FanDuel as pure DFS providers.[128] Since 2016, DraftKings and FanDuel have offered "Leagues" and "Friends Mode," respectively.[129] These features "give[] users the ability to play against a single group of friends all season long" and demonstrate a clear "foray into the . . . season-long market."[130] Because DraftKings and FanDuel both offer competitions that directly compete with traditional SLFS, the argument that these companies operate in a separate DFS market loses force.[131]

In the end, the differences between DFS and SLFS are not as drastic as the FTC suggests.[132] Therefore, the Commission erred when it concluded SLFS are not a part of the DFS market for merger analysis purposes.[133] As a result of this mistake, the FTC defined the relevant product market too narrowly.[134] This led the FTC to incorrectly conclude the Merger would result in a highly concentrated market, triggering the presumption of illegality.[135] This critical mistake is evidence that the Guidelines are implicating mergers that should be left unchallenged, which means the Guidelines are not serving their purpose and need to be revised.[136]

B. Dismissing Important Countervailing Factors

The Commission also ignored significant countervailing factors that militate against challenging the Merger.[137] Subsection 1 explains how the Merger would have eliminated regulatory uncertainty in the DFS industry, thereby making entry into the market more likely.[138] Subsection 2 describes how the Merger would have generated significant cost-saving efficiencies consumers likely would have benefitted from.[139]

1. The Merger Would Have Eliminated the Regulatory Uncertainty Barrier to Entry

The FTC found entry into the DFS market would not "be timely, likely, and

128. Daniel Roberts, *DraftKings, FanDuel, Yahoo Dip Their Toes into Season-Long Fantasy Sports*, YAHOO FIN. (Aug. 14, 2016), https://finance.yahoo.com/news/draftkings-leagues-fanduel-dfs-daily-000000742.html (on file with *The University of the Pacific Law Review*).

129. *Id.*

130. *Id.*

131. *Id.*

132. *Id.*

133. *Id.*

134. Complaint, DraftKings, Inc. (dismissed July 14, 2017) (No. 9375), 2017 WL 3049123 (F.T.C.), at *6.

135. *Id.*

136. *Id.*

137. Heitner, *supra* note 2.

138. *Infra* Part IV.B.1.

139. *Infra* Part IV.B.2.

sufficient to offset the anticompetitive effects of the Merger."[140] The FTC reasoned that high regulatory compliance costs and significant regulatory uncertainty in the industry made market entry an inadequate offset.[141] As a consequence of blocking the Merger, however, the FTC entrenched uncertainty in the DFS industry because DraftKings and FanDuel cannot effectively collaborate on lobbying for industry regulations as separate entities.[142] Without synergy and collaboration between these companies on this issue, alleviating the regulatory uncertainty in the industry becomes much less likely, which discourages prospective firms from entering the market.[143]

On the other hand, if the Commission had approved the Merger, it would have helped eliminate the industry's regulatory uncertainty, thereby increasing the likelihood of market entry and fostering a more competitive environment.[144] The Merger would have created a more stable regulatory environment because the merged firm would be able to "work more efficiently and economically with state government officials to develop a standard regulatory framework for the industry."[145] The major motivations behind the proposed Merger were reducing compliance costs and creating a consistent regulatory framework, so eliminating regulatory uncertainty would have been a likely result of the Merger.[146] Finalizing a regulatory framework would have reduced the legal and lobbying expenses that have had a debilitating effect on each company's bottom line.[147]

Assuming a merged DraftKings and FanDuel would accomplish its goal of eliminating regulatory uncertainty and reducing compliance costs, all other firms in the DFS market would benefit from a more stable and attractive regulatory environment.[148] This attractive environment would encourage prospective firms to enter the industry, creating a more competitive marketplace.[149] The FTC ensured hostility to market entrants by blocking the Merger, whereas approving the Merger would have fostered a more competitive environment by eliminating the most significant barrier to entry.[150]

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140. Complaint, DraftKings, Inc. (dismissed July 14, 2017) (No. 9375), 2017 WL 3049123 (F.T.C.), at *13.

141. *Id.*

142. Heitner, *supra* note 2; Purdum, *supra* note 3.

143. *A Merger Borne of Weakness*, ECONOMIST (Nov. 24, 2016), https://www.economist.com/blogs/gametheory/2016/11/daily-fantasy-sports (on file with *The University of the Pacific Law Review*).

144. *Id.*

145. Heitner, *supra* note 2.

146. *Id.*; *see also* Erin Griffith, *5 Things to Know About the Failed FanDuel-DraftKings Merger*, FORTUNE (July 14, 2017), http://fortune.com/2017/07/14/5-things-to-know-about-the-failed-fanduel-draftkings-merger/ (on file with *The University of the Pacific Law Review*) (elaborating on the uncertainty both DraftKings and FanDuel face after terminating the Merger).

147. Heitner, *supra* note 2; *see also* Griffith, *supra* note 146.

148. Heitner, *supra* note 2; *see also* Griffith, *supra* note 146 (explaining that the Merger "was supposed to reduce the amount of resources the companies were spending on regulatory issues").

149. Heitner, *supra* note 2.

150. *Id.*; Complaint, DraftKings, Inc. (dismissed July 14, 2017) (No. 9375), 2017 WL 3049123 (F.T.C.), at *14.

2. The Merger Would Have Created Cost-Saving Efficiencies

The FTC also contended there were no cognizable efficiencies that would counterbalance the Merger's anticompetitive effects.[151] However, a merged DraftKings and FanDuel would likely enjoy enormous cost savings, which is a significant efficiency.[152] As separate entities, DraftKings and FanDuel are "doubling the resources spent on legal battles" and advertising.[153] For example, in 2015, DraftKings and FanDuel spent a combined $500 million on advertising.[154] While both companies have reduced their advertising budgets since, the Merger would have allowed the combined company to decrease advertising expenditures even further.[155] Similarly, as separate firms, DraftKings and FanDuel have redundant legal and lobbying expenses.[156] A merged company would eliminate redundant costs and allow for more efficient work with government officials.[157]

DraftKings and FanDuel ultimately pass their significant advertising and legal costs on to consumers.[158] Therefore, consumers would likely benefit from the merged firm's ability to reduce costs.[159] The merged company may try to retain all cost savings to increase profits, but some benefits would likely extend to consumers as well.[160] For example, cost savings could benefit consumers by making DFS contests cheaper for players.[161] Additionally, the increased likelihood of market entry after the Merger could incentivize the merged company to invest its cost savings in product innovation.[162]

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151. *Id.*

152. Griffith, *supra* note 146; *see also* Heitner, *supra* note 2 (describing cost savings associated with increased efficiency and the ability to be more sustainable if the companies merged). *See generally* Diane Bartz, *FanDuel, DraftKings Scrap Troubled Merger*, REUTERS (July 13, 2017), https://www.reuters.com/article/us-fanduel-m-a-draftkings/fanduel-draftkings-scrap-troubled-merger-idUSKBN19Y2KL (on file with *The University of the Pacific Law Review*) (determining that without the merged companies, each individual company will have to spend to compete with one another).

153. Griffith, *supra* note 146.

154. Alexandra Berzon, *Fantasy-Sports Sites Curtail Ad Spending*, WALL ST. J. (Aug. 1, 2016), https://www.wsj.com/articles/fantasy-sports-rivals-slice-ad-spending-1470052800 (on file with *The University of the Pacific Law Review*).

155. *Id.*

156. Griffith, *supra* note 146; Bartz, *supra* note 152.

157. Heitner, *supra* note 2; *see also* Bartz, *supra* note 152 (explaining that a purpose of the Merger was to reduce redundant costs).

158. Griffith, *supra* note 146.

159. *Statement from FanDuel CEO Nigel Eccles on Termination of Merger*, FANDUEL (July 13, 2017), https://newsroom.fanduel.com/2017/07/13/statement-from-fanduel-ceo-nigel-eccles-on-termination-of-merger/ (on file with *The University of the Pacific Law Review*).

160. Timothy J. Muris & Bilal Sayyed, *Three Key Principles for Revising the Horizontal Merger Guidelines*, ANTITRUST SOURCE 7 (Apr. 2010), *available at* https://www.americanbar.org/content/dam/aba/publishing/antitrust_source/Apr10_Muris4_14f.authcheckdam.pdf (on file with *The University of the Pacific Law Review*).

161. Griffith, *supra* note 146; *see also* Muris & Sayyed, *supra* note 160, at 7.

162. *See Statement from FanDuel CEO Nigel Eccles on Termination of Merger*, *supra* note 159

Thus, the Commission appears to have ignored a significant efficiency that would counteract the anticompetitive effects of the Merger by dismissing the Merger's ability to reduce fixed costs.[163] Rather than leading to higher prices and reduced innovation, the Merger likely would have benefitted consumers because the merged firm could have realized hundreds of millions of dollars in cost savings.[164]

V. CHANGING THE GAME: REVISING THE HORIZONTAL MERGER GUIDELINES

The numerous missteps in the FTC's analysis of the Merger indicate the necessity of revising the Guidelines.[165] Revisions will help the FTC more effectively carry out its mandate to ensure markets remain competitive, enforce antitrust laws, and promote consumer welfare.[166] Further, these revisions will help prevent the Commission from unnecessarily challenging harmless merger proposals in the future.[167] Section A proposes leveling the burden of proof for merger efficiencies.[168] Section B suggests the Guidelines should acknowledge that consumers benefit from a merged firm's fixed cost savings.[169] Section C recommends removing innovation from the competitive effects analysis.[170] Section D advocates eliminating the presumption of illegality from the Guidelines.[171]

A. Leveling the Burden of Proof for Merger Efficiency Claims

One way to improve the effectiveness of the Guidelines is to level the burden of proof for merger efficiency claims.[172] Currently, the Guidelines do not provide for a difference between the burden of proof required to establish efficiency claims or anticompetitive effects.[173] In reality, however, the Commission's "investigating attorneys appear more skeptical of efficiency claims than they do

(expecting benefits to customers through increased investment in growth and product development).

163. Griffith, *supra* note 146.

164. *See* Berzon, *supra* note 154 (describing DraftKings' and FanDuel's spending of millions of dollars in competition, leading to operating losses for both companies); *see also* Griffith, *supra* note 146 (explaining that after the Merger, reducing costs would lower prices for customers).

165. *See* Press Release, *Department of Justice and Federal Trade Commission Issue Revised Horizontal Merger Guidelines*, DEP'T OF JUST. (Aug. 19, 2010), https://www.justice.gov/opa/pr/department-justice-and-federal-trade-commission-issue-revised-horizontal-merger-guidelines (on file with *The University of the Pacific Law Review*) (introducing techniques and methods to assess the effects of horizontal mergers).

166. *Id.*; *What We Do*, *supra* note 12.

167. Press Release, *supra* note 165.

168. *Infra* Part V.A.

169. *Infra* Part V.B.

170. *Infra* Part V.C.

171. *Infra* Part V.D.

172. Muris & Sayyed, *supra* note 160, at 7.

173. *Id.*

of potential anticompetitive effect claims."[174] Additionally, the Guidelines require merging firms to prove efficiency claims in great detail.[175] In contrast, the FTC does not have to precisely substantiate anticompetitive effects because the Guidelines state "that certainty about anticompetitive effect is seldom possible."[176] This distinction implicitly suggests there is a higher burden of proof for efficiency claims.[177]

The FTC should revise its Guidelines to "explicitly reject different burdens of proof for procompetitive and anticompetitive effects."[178] Doing so would promote more consistent application of the Guidelines and encourage the Commission to more seriously consider efficiency claims, rather than quickly and skeptically dismiss them.[179]

B. Acknowledging Fixed Cost Reductions Benefit Consumers

The FTC should also revise the Guidelines to more fully address fixed cost savings as cognizable efficiencies consumers benefit from.[180] Currently, the FTC limits its discussion of fixed cost savings as efficiencies to a skeptical footnote in the Guidelines.[181] The Merger would have resulted in considerable savings on advertising and legal expenses, yet the FTC did not recognize the savings as a cognizable efficiency in its complaint.[182] The Commission likely did not recognize the cost savings as a cognizable efficiency because the Guidelines currently state that "[e]fficiencies relating to costs that are fixed in the short term are unlikely to benefit customers in the short term."[183] The FTC "normally give[s] the most weight to the results . . . over the short term."[184] Many companies, however, establish their price structures using their total costs, which include fixed costs.[185] This means that when fixed costs decrease for these companies, prices will as well.[186] As a result, the FTC should reconsider its position in the Guidelines that efficiency claims based on fixed costs savings are not entitled to much weight.[187]

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174. *Id.*

175. GUIDELINES, *supra* note 11, at 30.

176. *Id.* at 1.

177. *Id.* at 1, 30.

178. Muris & Sayyed, *supra* note 160, at 7.

179. *See id.* (concluding that the application of a uniform burden of proof would result in consistency).

180. *Id.* at 6.

181. GUIDELINES, *supra* note 11, at 31.

182. Griffith, *supra* note 146; Complaint, DraftKings, Inc. (dismissed July 14, 2017) (No. 9375), 2017 WL 3049123 (F.T.C.), at *14.

183. GUIDELINES, *supra* note 11, at 31.

184. *Id.*

185. Muris & Sayyed, *supra* note 160, at 7.

186. *Id.*

187. GUIDELINES, *supra* note 11, at 31; *see also* Muris & Sayyed, *supra* note 160, at 9 (suggesting methods to revise Guidelines).

Even if there are few industry competitors remaining after a merger, a merged firm is still likely to pass some of its fixed cost savings along to consumers.[188] Therefore, concerns that a concentrated marketplace will prevent consumers from enjoying lower prices generated by a merged firm's fixed cost savings should not keep the FTC from adopting this revision.[189]

Adopting this revision would better align the Guidelines with the Commission's actual practices.[190] In practice, the FTC is "as likely to accept fixed-cost savings as [it is] to accept claims of variable-cost savings."[191] This demonstrates a significant disconnect between the Guidelines and actual FTC practices.[192] Because of this disconnect, discerning how the FTC will evaluate the fixed cost savings that result from a merger becomes much more difficult.[193] When such a disconnect exists, the Guidelines cease to achieve one of their primary goals—providing transparent FTC antitrust enforcement.[194] For these reasons, the FTC should more receptively address claims of fixed cost savings as cognizable efficiencies by revising the Guidelines.[195]

C. Removing the Effect on Innovation from the Competitive Effects Analysis

Removing the innovation analysis could also increase the Guidelines' effectiveness.[196] Currently, the Guidelines recognize that reduced innovation could be an anticompetitive effect of a merger and that increased innovation could also be an efficiency resulting from a merger.[197] Determining a merger's effect on innovation can be extremely difficult because "the competition-innovation link is neither settled nor supportive of a causal relationship between the number of firms and amount of (successful) innovation."[198] It is unclear how an industry's competitive environment affects a firm's ability and incentive to innovate.[199]

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188. *Id.*

189. *Id.*

190. MALCOM B. COATE & ANDREW J. HEIMERT, FED. TRADE COMM'N, ECONOMIC ISSUES: MERGER EFFICIENCIES AT THE FEDERAL TRADE COMMISSION 1997–2007 vi (2009), *available at* https://www.ftc.gov/sites/default/files/documents/reports/merger-efficiencies-federal-trade-commission-1997–2007/0902mergerefficiencies.pdf (on file with *The University of the Pacific Law Review*).

191. *Id.*

192. *Compare* GUIDELINES, *supra* note 11, at 31 (describing unpredictable results due to difficulties with verification), *with* COATE & HEIMERT, *supra* note 190, at vi (explaining the Bureau of Competition's and the Bureau of Economics' results in evaluating efficiency claims).

193. *Compare* GUIDELINES, *supra* note 11, at 31 (describing unpredictable results due to difficulties with verification), *with* COATE & HEIMERT, *supra* note 190, at vi (explaining the Bureau of Competition's and the Bureau of Economics' results in evaluating efficiency claims).

194. GUIDELINES, *supra* note 11, at 1.

195. Muris & Sayyed, *supra* note 160, at 6.

196. *Id.* at 12.

197. GUIDELINES, *supra* note 11, at 23, 31.

198. Muris & Sayyed, *supra* note 160, at 12.

199. *See id.* (describing how the fact-intensive determinations regarding innovation create uncertain and

Further, the FTC lacks experience with evaluating innovation.[200] The experience the FTC does have "derive[s] from investigations of mergers in the pharmaceutical industry," which may not be helpful when analyzing a merger's effect on innovation in other industries.[201] With the limited knowledge of a merger's effect on innovation and the Commission's inexperience with analyzing innovation, the Commission should revise the Guidelines to remove the innovation analysis.[202]

D. Eliminating the Presumption of Illegality

Finally, eliminating the presumption of illegality for mergers reaching specific HHI thresholds could help the Guidelines become more effective and transparent.[203] The presumption of illegality is problematic for multiple reasons.[204] First, HHI scores derive directly from product market definition.[205] The powerful effect of a presumption of illegality thus forces the merging parties and the FTC to dedicate too much effort to defining the relevant product market.[206] As a result, the merging parties and the FTC may lose focus on analyzing other specific circumstances that shed light on a particular merger's likely competitive effects.[207] The presumption of illegality has a significant unintended consequence of distorting the breadth and depth of merger analysis.[208]

Additionally, similar to efficiency claims for fixed cost savings, the Commission's practice regarding the presumption of illegality has not always aligned with the Guidelines.[209] This divergence between agency practice and the Guidelines leads to confusion for businesses and makes the Guidelines less transparent.[210] Therefore, removing the presumption of illegality from the Guidelines and agency practice will improve consistency and provide greater clarity to merging companies.[211]

Further, the presumption of illegality compounds the burden of proof problem that permeates the Guidelines.[212] Already having the burden to prove merger efficiencies in great detail, merging parties must rebut the presumption of

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unpredictable results).

200. *Id.*

201. *Id.*

202. *See id.* (discouraging the inclusion of innovation in the Guidelines).

203. John Harkrider, *Proving Anticompetitive Impact: Moving Past Merger Guidelines Presumptions*, 2005 COLUM. BUS. L. REV. 317, 333 (2005).

204. *Id.* at 332–33.

205. GUIDELINES, *supra* note 11, at 7.

206. Harkrider, *supra* note 203, at 330.

207. *Id.* at 333.

208. *Id.*

209. Muris & Sayyed, *supra* note 160, at 5.

210. Harkrider, *supra* note 203, at 324.

211. *Id.* at 333.

212. GUIDELINES, *supra* note 11, at 19.

illegality "by persuasive evidence showing that the merger is unlikely to enhance market power."[213] As a result, after the FTC proves that a merger would reach the appropriate HHI thresholds, the merging parties have the burden to prove the merger's efficiencies and disprove its anticompetitive effects.[214] The presumption of illegality places an enormous burden on the merging parties.[215]

In the end, the Commission should revise the Guidelines to eliminate the presumption of illegality when mergers reach certain HHI levels.[216] The Guidelines should only indicate that when a merger attains a particular HHI threshold, the FTC will engage in a more detailed investigation into the merger's likely competitive effects.[217] Such a revision will ensure the Commission engages in "a more direct analysis of likely competitive effects" that could result from a merger.[218] Even with this revision, the HHI can continue "provid[ing] substantial guidance as highly useful screens."[219]

VI. CONCLUSION

The FTC's decision to challenge the DraftKings and FanDuel merger directly impacts roughly three million active players on these sites and leaves the future of these companies and the DFS industry in doubt.[220] Ultimately, one of these companies may go out of business, which would produce the exact monopoly in the DFS industry the Commission argued it avoided creating by challenging the Merger.[221] Consumers should have significant concerns about their ability to enjoy DFS games in the future.[222]

The implications of the Commission's decision to block the Merger extend far beyond the DFS industry.[223] If the current version of the Guidelines led the FTC to unnecessarily block the Merger, the Guidelines could likewise direct the FTC to needlessly challenge other mergers in the future.[224] When the Commission challenges mergers it should actually approve, the Commission is not effectively carrying out the mandates established in the FTC Act and the

213. *Id.*

214. *Id.*

215. Harkrider, *supra* note 203, at 319.

216. *Id.* at 333.

217. Muris & Sayyed, *supra* note 160, at 6.

218. *Id.* at 5.

219. *Id.*

220. *See* Daniel Roberts, *The Growth in Fantasy Sports Will Not Come from Football*, YAHOO FIN. (Sept. 28, 2017), https://finance.yahoo.com/news/growth-fantasy-sports-will-not-come-football-124020874.html (on file with *The University of the Pacific Law Review*) (providing only three out of ten million registered DFS users are active).

221. *See* Purdum, *supra* note 3.

222. *Id.*

223. GUIDELINES REVIEW PROJECT TRANSCRIPT, *supra* note 31, at 15.

224. *See id.* (describing the Guidelines as having "the most important influence in American antitrust policy in the last 50 years").

Clayton Act.[225] Instead, the FTC causes the exact harm these laws entrust the FTC to prevent.[226]

For these reasons, the failed DraftKings and FanDuel merger is an important signal that it is time to revise the Guidelines once again.[227] Simple revisions like leveling the burden of proof for the FTC and merging parties and eliminating the presumption of illegality can make the Guidelines and antitrust enforcement more effective.[228] Similarly, removing innovation from the competitive effects analysis and fully recognizing fixed cost savings as a cognizable efficiency can improve the Guidelines.[229] By taking these steps, the Commission can ensure it is protecting consumers, being transparent with businesses, and minimizing its interference with mergers that will not harm, but may in fact benefit, consumers.[230]

225. 15 U.S.C.A. §§ 18, 45(a)(1)–(2) (Westlaw through Pub. L. No. 115-72).

226. *Id.*

227. FANTASY SPORTS TRADE ASSOCIATION, *supra* note 112, at 12; Press Release, *supra* note 165.

228. Harkrider, *supra* note 203, at 319, 333; Muris & Sayyed, *supra* note 160, at 4, 7.

229. Muris & Sayyed, *supra* note 160, at 12.

230. *See What We Do*, *supra* note 12 (explaining one of the purposes of the FTC is to "protect customers"); *see also* Press Release, *supra* note 165 (emphasizing agency goals of decreasing interference with competitively beneficial mergers). *See generally* GUIDELINES, *supra* note 11, at 1 (describing increased transparency resulting from use of the Guidelines).